

General Information Letter: Installation services provided by the taxpayer would not be protected by Public Law 86-272.

March 14, 2003

Dear:

This is in response to your letter dated February 20, 2003, in which you request information. Department of Revenue ("**Department**") regulations require that the Department issue only two types of letter rulings, Private Letter Rulings ("**PLRs**") and General Information Letters ("**GILs**"). **PLRs** are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A **PLR** is binding on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the **PLR** are correct and complete. **GILs** do not constitute statements of agency policy that apply, interpret or prescribe the tax laws and are not binding on the Department. For your general information, the regulation governing the issuance of letter rulings, 2 Ill. Adm. Code Part 1200 regarding rulings and other information issued by the Department, can be accessed at the Department's website. That address is [www.revenue.state.il.us/legalinformation/regs/part1200](http://www.revenue.state.il.us/legalinformation/regs/part1200).

The nature of your correspondence and the information provided require that we respond only with a **GIL**.

In your letter you state in part as follows:

The reason for this letter is to ask for your assistance in verifying Illinois income tax nexus for COMPANY1, a member of the consolidated return of COMPANY2 and subsidiaries (XX-XXXXXXX). We have been filing returns in recent years and believe doing so correctly. The following discussion will provide an overview and explanation of COMPANY1's situation, and a specific request for your assistance.

COMPANY1 is in business to provide superior custom-engineered products and services to customers requiring space enhancement storage solutions to storage, material handling, and environmental needs. COMPANY1 primarily engineers, sells, manufactures and installs three distinct product lines throughout the United States. They are: PRODUCT1s, PRODUCT2s, and PRODUCT3. In the case of PRODUCT1s, each customer seeks additional vertical space for handling or storing materials. In the case of PRODUCT2s, customers are looking for efficiencies in handling or moving materials. Finally, in the case of PRODUCT3, customers are looking to protect their assets from damage and repair. All three product lines are directly associated with the INDUSTRY.

COMPANY1 conducts business through a core group of independent material handling dealers across the United States that handle our products along with other manufacturer's products. We have approximately 200 active dealers at any given time in the U.S. It is their job to find customers who have a need that we can fill. In the majority of cases, the dealer will get an inquiry from a potential customer. COMPANY1 quotes the order and the dealer generates a purchase order if the customer accepts the quote. COMPANY1 manufactures the product at their Wisconsin facility and drop ships to end user. COMPANY1 invoices the dealer who then resells the product to the customer. In ten to twenty percent of orders, COMPANY1 will send engineers out to the site for field measurements in order to retrofit an existing space, send a subcontract

vendor to do the install, or send an installation manager to the site for coordination, supervision or inspection.

It has been determined several years ago by our accountants, consultants, and legal counsel that these business activities created sales and use tax nexus as well as income tax nexus in the majority of the states where COMPANY1 does ongoing business. COMPANY1 registered for sales and use tax in your state at that time and has since been filing sales and use tax returns and income tax returns as directed by your state laws. For the years 1998 through 2000, sales to Illinois totalled \$X,XXX,XXX. Included in this total are installation sales of \$XXX,XXX. COMPANY1 is currently under audit by the Wisconsin Department of Revenue and needs **immediate proof of nexus** with those states where it is included in either parent consolidate or unitary income tax returns. The WI Department of Revenue requires as one form of proof a letter from your state on official State letterhead in order to substantiate our nexus claim for income tax. We respectfully ask you to assist us in providing a letter of this nature. We realize it is difficult to fully advise you of COMPANY1's Illinois business activities in a brief letter. Mr. Z, COMPANY1's Controller will be available, at your convenience, to discuss further details. If necessary, we will provided more written information and details in order for you to feel comfortable in honoring this request.

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If we do not receive anything from your state, we will assume that you have no requirements for the reporting of miscellaneous income or for the withholding from payments for services to non-employees... If your state has no requirements for this type of information reporting please complete the attached form...

In response to your inquiry, please be advised that the determination of whether a taxpayer has nexus with the State of Illinois is extremely fact-specific. Such a determination can be made only in the context of an audit where a Department auditor has access to all relevant facts and information. However, we can provide you general information regarding income tax nexus with the state.

Section 201 of the Illinois Income Tax Act (**IITA**), 35 ILCS 5/201 imposes a tax measured by net income on corporations for the privilege of earning or receiving income in this State. The Due Process and Commerce Clauses of the Federal Constitution limit the power of states to subject foreign corporations to tax. The Due Process Clause requires that there be some minimum connection between a state and the person, property, or transaction it seeks to tax (Quill Corp. v. North Dakota, 504 U.S. 298, 112 S. Ct. 1904 (1992)). Similarly, the Commerce Clause requires that the tax be applied to an activity with a substantial nexus to the taxing state. Id. Where any part of a foreign corporation's income is allocable to Illinois in accordance with the provisions of Article 3 of the IITA, Illinois can demonstrate the connection or nexus necessary to subject a foreign corporation to tax. Therefore, unless protected by Public Law 86-272, a foreign corporation is liable for Illinois income tax where any part of its income is allocated to Illinois. Furthermore, under regulations promulgated by the Department which interpret the foregoing principles of law, Illinois has adopted the "Joyce" rule regarding the establishment of nexus in the case of separate members of a unitary business group. Specifically, this rule provides

f) Application of the Joyce rule. In determining whether the activity of a nonresident taxpayer conducted in this State is sufficient to create nexus for application of Illinois income or replacement tax, the principles established in Appeal of Joyce, Inc., Cal. St. Bd. Of Equal. (11/23/66), commonly known as the "Joyce rule", shall apply. Only activity conducted by or on behalf of the nonresident taxpayer shall be considered for this purpose. Because the income of a partnership, a Subchapter S corporation or any other pass-through entity is treated as income of the owners, activity of a pass-through entity is conducted on behalf of its owners. Activity conducted by any other person, whether or not affiliated with the nonresident taxpayer, shall not be attributed to the taxpayer, unless the other person was acting in a representative capacity on behalf of the taxpayer.

Additionally, subsection c) 6) of that regulation provides as follows:

- 6) Independent Contractors. PL 86-272 provides immunity to certain in-state activities, if conducted by an independent contractor, that would not be afforded if performed by the nonresident or its employees or other representatives.
- A) Notwithstanding the provisions of subsection (c)(4), independent contractors may engage in the following limited activities in the State without the nonresident's loss of immunity:
- i) soliciting sales;
  - ii) making sales;
  - iii) maintaining an office.
- B) Sales representatives who represent a single principal are not considered to be independent contractors and are subject to the same limitations as those provided under PL 86-272 and this Section.
- C) Maintenance of a stock of goods in the State, by the independent contractor under consignment or any other type of arrangement with the nonresident, except for purposes of display and solicitation, shall remove the protection.

In addition, IITA Section 304 provides for taxable years ending on or after 12/31/00 that the apportionment factor for a foreign corporation deriving business income from Illinois and one or more other states shall be equal to its sales factor. Section 304(a)(3)(A) defines the sales factor as a fraction, the numerator of which is the total sales of the person in Illinois during the taxable year, and the denominator of which is the total sales of the person everywhere. Department of Revenue Regulations Section 100.3700(c)(1) states that gross receipts from sales of tangible personal property are allocable to Illinois for sales factor purposes if the property is delivered or shipped to a purchaser within this state regarding of the f.o.b. point or other conditions of sale.

Your letter states that COMPANY1 conducts business through a core group of independent material handling dealers across the United States that handle its product along with other manufacturer's products. It then quotes the price for a particular item of tangible personal property through local dealers to prospective customers. If the customer accepts the quote, COMPANY1 then manufactures the product at its Wisconsin facility and drop ships it to the end user. COMPANY1 invoices the dealer who/which then resells the product to the customer. Furthermore, you state, "in ten to twenty percent of orders, COMPANY1 will send engineers out to the site for field measurements in order to retrofit an existing space, send a subcontract vendor to do the install, or send an installation manager to the site for coordination, supervision or inspection."

As stated above, Revenue does not make definitive determinations of nexus by means of letter rulings. Given the few facts presented, it appears that the sales transactions described might very well be covered by the "independent contractor" provisions of PL 86-272. However, the fact that COMPANY1 regularly and periodically assists in the installation of the product it sells, as well as performing other related services, would take it out of protected status by virtue of Regulation Section 100.9720(c)(4)(D) installation, (F) providing technical assistance/service, and (S) conducting non-protected, non-ancillary activities.

As stated above, this is a **GIL** which does not constitute a statement of policy that applies, interprets or prescribes the tax laws, and it is not binding on the Department. If you wish to obtain a **PLR** which will bind the Department with respect to the application of the law to specific facts, please submit a request conforming to the requirements of 2 *Ill. Adm. Code Part 1200*.

Sincerely yours,

Jackson E. Donley,  
Senior Counsel-Income Tax